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SUBJECT: GOU CRITICAL OF MERCOSUR BUT STILL INTENDS TO  
REMAIN MEMBER AND NEGOTIATE WAIVER FOR FTA WITH U.S.

Classified By: Charge D'Affaires James D. Nealon  
for reasons 1.4 (B) and (D)

11. (C) Summary: Harsh criticism of Mercosur continues unabated in Uruguay, fueled by a worsening dispute with Argentina, Brazil's distraction with regional events, and an increased marginalization of Mercosur's smaller members in the decision-making. The trade bloc could tilt towards a more political entity if Mercosur accepts Venezuela's proposal to become a full member without having to adhere to the Common External Tariff (CET) and implement intra-zone free trade as pre-conditions. For its part, the GOU is pushing Mexico's long-standing request for associate membership to balance out Brazil's influence.

2.(C) Meanwhile, public discussion of a possible Free Trade Agreement (FTA) with the U.S. continues to be widely debated and support for the initiative is gathering strong momentum. There is broad consensus that the best option is for Uruguay to negotiate a waiver with its Mercosur partners. The Paraguayan and Argentine presidents have publicly stated they would agree to this waiver. An unusual mea culpa from the Brazilian Foreign Minister about his country's lack of attention to Mercosur's smaller members may be a prelude to a similar gesture from Brazil. President Vazquez recently stated that he wants Uruguay to open up to the world the way Chile has. He plans over the next couple of years to start FTA negotiations with other major markets, such as the EU, China and India. The following assessment is based on recent discussions with Mercosur Secretariat and GOU officials dealing with Mercosur issues. End Summary.

Continued criticism of Mercosur  
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13. (U) Politicians, editorialists and business leaders continue to vent steady criticism about Mercosur's failures and to question its relevance for Uruguay. The widening debate was exacerbated lately by a worsening of the dispute with Argentina over pulp mills, Argentina's refusal to call a special meeting of Mercosur Common Council to address the issue, and Brazil's hands-off posture in the conflict. Economy

Minister Astori commented that Mercosur is undergoing its most severe crisis and is working "against Uruguay's economic interests". Among the bloc's shortcomings, he highlighted the passage of the Argentine/Brazilian safeguard mechanism and Mercosur's failure to conclude trade agreements with any significant partners. In an unusual move for Uruguay's traditionally quiet private sector, the four largest and most influential business chambers issued a joint statement very critical of the trade bloc.

14. (C) The increasing marginalization of Uruguay by Mercosur's larger countries is taking a toll even within sectors traditionally favorable to regional integration, such as the Uruguayan Ministry of Foreign Affairs. MFA officials told us they are incensed by a proposal floated by Venezuela and allegedly supported by Brazil, which would grant it special treatment to facilitate its entry into Mercosur. According to this proposal, to be outlined next week at a Mercosur meeting, Venezuela would not have to adhere to the Common External Tariff nor implement intra-zone free trade prior to admission, but would utilize an ALADI agreement (ACE #59) instead. Venezuela would gain full membership by subscribing to the Declaration of Asuncion and a series of Mercosur norms. In the view of these officials, what they perceived as a blatant double-standard confirmed once more that Mercosur's obligations apply only to smaller members, while larger countries bend the rules at will for their own benefit (Note: President Vazquez has repeatedly complained about a Mercosur with "first-class" and second-class" members. End Note.)

15. (C) If Venezuela were to be admitted as a full member under these conditions, it could signal a trend towards a more political entity and a shift from an imperfect customs union to more of a political bloc. Still, high-level officials at the Mercosur Secretariat doubted that the Venezuelan proposal would go very far and be approved by all members. They saw it as a sign of the GOV's inexperience in international trade negotiations and were quite dismissive of the technical capacity of the Venezuelan delegations to Mercosur meetings: "They love to talk but are totally useless."

16. (C) Mercosur did not put up a good show at the recent Latin American-European Summit in Vienna, as little or no progress on trade issues emerged from the Mercosur/EU talks. The meeting was plagued by conflicts and tensions among several South American leaders. The local press relayed the image of a deeply divided continent, split between "serious" governments and populists, in an encounter with EU governments more concerned about safeguarding their respective investments in Latin America than building up relationships. As with other Mercosur trade negotiations, talks with the EU have historically been led and managed by the GOB. According to GOU officials, part of the failure of these latest talks lay squarely with Brazil's current state of distraction with regional events (the nationalization of gas in Bolivia and Chavez's push for regional leadership) and its resulting lack of focus on Mercosur's trade issues.

A Brazilian mea culpa

17. (U) On May 9, Brazil's Foreign Affairs Minister Celso Amorim reportedly admitted before his Senate's Foreign Affairs Commission that the GOB "has not done enough for Paraguay and Uruguay" and "especially for Uruguay that is now uncomfortable with Mercosur". Calling for a more generous" policy towards its neighbors --one that includes credit and increased purchases of goods-- Amorim concluded that the GOB "has talked a lot but delivered little." In an interview with the respected Uruguayan weekly Busqueda, President Lula's Special Advisor Marco Aurelio Garcia said that the possibility of Uruguay leaving Mercosur is a "fundamental concern" for President

Lula. It would be a "large loss" for the bloc and would signify a "resounding failure of Mercosur" in dealing with smaller partners.

A growing lobby for bilateral trade agreements...

18. (U) The discontent in Uruguay with Mercosur has led to renewed calls for an opening to outside trade partners through bilateral trade agreements. Astori, one of the most active proponents of an FTA with the U.S., stated that the GOU needs "more than ever, to improve its international position outside the region". This vision is shared by the four major Uruguayan business chambers, which recently published a study entitled "Joint Position on the Convenience of Negotiating Trade Agreements with Extra-Zone Countries". Vazquez has stated repeatedly that he wants Uruguay to open up to the outside world in the same way as Chile has done. He has outlined plans to open negotiations over the next couple of years on an ambitious series of FTAs with other major markets besides the U.S., such as the EU (if Mercosur-EU talks continue to show no progress), China and India. On May 19, Astori confirmed that initial contacts with the governments of China and India had been positive.

...but a commitment to remain within Mercosur

19. (U) Still, despite strong repeated criticism of Mercosur, broad consensus remains that the GOU's first-best alternative for bilateral free trade talks is to negotiate a waiver from its Mercosur partners. Astori openly rejected the idea of leaving Mercosur or turning into an associate partner, which he considered would be an extremely grave mistake". As for Vazquez, he has maintained pressure through a barrage of criticism of Mercosur's weaknesses and failures, but has made clear that Uruguay's future remains within the trading bloc. We want a stronger and better Mercosur", is his mantra. Following his trip to Mexico, Vazquez said that Uruguay would advocate for Mexico's long-standing request for associate membership into Mercosur as a counterweight to Brazil.

Comment: Good prospects of Mercosur waiver for FTAs

10. (C) Vazquez's vision is that of an opening to the outside world, and Chile is clearly his model: "Uruguay is seen as a very serious and responsible country, as is Chile." The GOU appears confident it will obtain the necessary waiver from its Mercosur partners to move forward with bilateral trade talks. Initial signals are positive. On May 10, Paraguayan President Duarte supported the GOU's initiative to negotiate a waiver and less than a week later, Argentine President Kirchner declared upon returning from Vienna that "one must be flexible (with Uruguay) and let them sign a free trade agreement with the U.S." While Brazil's Lula has not yet opined on the matter, the signals from the Brazilian MFA about the importance of maintaining Uruguay within Mercosur may point the way to a positive reply. End Comment.  
Nealon